United States Court of Appeals

for the Second Circuit

APPELLEE'S BRIEF

No. 76-7414

In the
United States Court of Appeals
For the Second Circuit

BRUNSWICK CORPORATION and SHERWOOD MEDICAL INDUSTRIES, INC., *Counterdefendants-Appellees,*	On Appeal from the United States District Court for the Northern District of New York.
vs.	
DAVID S. SHERIDAN and NATIONAL CATHETER CORPORATION, *Counterclaimants-Appellants.*	Honorable **James T. Foley,** Judge Presiding

BRIEF FOR APPELLEES

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BRIEF FOR APPELLEES

DECISION BELOW

At the close of the evidence the District Court directed a verdict in favor of plaintiffs Brunswick and Sherwood Medical Industries ("Sherwood") on Counts I, III and IV of the counterclaim, and submitted plaintiffs' claim (that defendants Sheridan and National Catheter Corporation[1] had violated a restrictive covenant in a May, 1971 settlement agreement) and the remaining count of the counterclaim to the jury, which was unable to agree on a verdict. The only question before this Court is whether the District Court acted properly in dismissing Count I of the counterclaim. (Appellants have abandoned their appeal

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1. Appellants David S. Sheridan and National Catheter Corporation are sometimes collectively referred to in this brief as "Sheridan." Appellees Brunswick and Sherwood Medical Industries are sometimes collectively referred to as "Sherwood."

from the directed verdicts on Counts III and IV (Appellants' Br. note 1).)*

STATEMENT OF ISSUES PRESENTED FOR REVIEW

1. Did the District Court correctly direct a verdict in favor of appellees with respect to a counterclaim charging violations of Section 1 of the Sherman Act on the ground that appellants had failed to present evidence of a "contract, combination or conspiracy" to restrain trade?

2. Did the District Court correctly direct a verdict in favor of appellees with respect to Section 2 of the Sherman Act on the ground that appellants had failed to present evidence of monopolization, attempted monopolization, or a combination and conspiracy to monopolize?

The four questions listed in appellants' Statement of Issues concerning patent misuse and the doctrine of ancillary restraints do not pertain to the questions raised by the direction of the verdict and, accordingly, need not be decided by this Court. Although appellants' arguments on these points lack merit, we do not wish to leave them unanswered, and they are considered in Points III and IV of this brief.

STATEMENT OF THE FACTS

Sheridan's statement of the facts contains a number of inaccurate statements and omits several significant facts. For these reasons we include our own statement of the facts.

The Product Involved in This Litigation

The product involved in this litigation is clear plastic tubing with a line of electrically conductive material running along its length. Sheridan refers to it as "conductive line tubing."

* The printed version of appellants' brief was unavailable at the time this brief was printed. Therefore, references herein are to the appropriate part or footnote in appellants' brief.

This tubing is connected to a suction machine during surgery to remove fluids from the patient's body. The conductive line prevents static electric discharges, which may prove hazardous in the presence of the flammable anesthetic gases sometimes used during surgery, by permitting the static electricity to flow along the tube to the machine or the floor (which is always made of metal) rather than cause a spark (App. 411-412, 450, 453, Pls. Ex. 14; App. 33, 50-51, 81-86, 97-99, Tr. 68, 93-94, 294-296, 316-317, 348-350).

In appellants' Statement of Facts and again in Part II-C, Sheridan asserts that another purpose of the conductive line is to eliminate the hazard of cardiac arrest as a result of "microshock." Microshock is the name given to the effect of small electric currents on the body; to create a hazard of cardiac arrest, the current must be applied to a conductor inside or in very close proximity to the heart (App. 408, 410, Pls. Ex. 14). There is no evidence in the record which in any way supports Sheridan's suggestion that suction tubing in general or Sherwood's tubing in particular creates any danger of microshock or that "conductive line" tubing is intended to eliminate any such danger.

The "conductive line" tubing produced by National Catheter (App. 392, Pls. Ex. 11) is nearly identical to that produced by Sherwood (App. 371, Pls. Ex. 4), and there is no discernible difference in the way the tubes perform in use. In the National Catheter tubing the conductive line rests on the outside surface of the tube in "piggyback" fashion whereas in the Sherwood tubing the conductive line is embedded in the plastic wall of the tube so that it forms part of both the inside and outside surface of the tube. The only other difference appears to involve different means of connecting lengths of tubing to each other. In any event, whether the two tubings are similar or dissimilar is relevant only to plaintiffs' complaint against Sheridan, and therefore is not an issue in Sheridan's appeal.

In addition to Sherwood and National Catheter, two other firms, Davol and Bard, manufacture and sell such tubing (App. 154, Tr. 971).

Factual Background

Some years ago Sheridan started his business, which was later sold to Brunswick, in a converted barn on his farm in North Argyle where he began developing techniques for extruding plastics to produce tubing for specialized medical purposes (App. 239-241, Tr. 1654-1656). Some years prior to 1960, Sheridan formed Sheridan Catheter and Instrument Corporation ("SCIC") to make and sell such tubing; in its early years SCIC continued to operate out of Sheridan's barn and was an extremely small operation (Appellants' Br. text at note 2; App. 49-50, Tr. 89-90). By 1960 its net worth had grown to only $95,442.00 (App. 343, Exhibit A to Pls. Ex. 2).

In 1959 John N. Willman, then the chief executive officer of Brunswick's Health and Science Division and later president of Sherwood, entered into negotiations with Sheridan which culminated in early 1960 with the execution of three contemporaneous agreements:

(1) A purchase agreement pursuant to which Brunswick purchased SCIC (App. 323, Pls. Ex. 2);[2]

(2) An employment agreement between Brunswick and Sheridan (App. 372, Pls. Ex. 5); and

(3) A license agreement pursuant to which Sheridan granted Brunswick exclusive rights under a number of patents, including several for which patent applications were pending, covering specialized medical tubing but not "conductive line" tubing (App. 348, Pls. Ex. 3).[3]

Under the employment agreement it was agreed that SCIC (or its successor) would employ Sheridan for 5 years with automatic

2. Under this Agreement Brunswick paid Sheridan actual net worth plus $99,401.00, or a total of $194,843.00.

3. The license agreement was amended in 1966 to cover patents and patent applications, including one for clear conductive tubing, issued or made while Sheridan was employed by Brunswick (App. 367, Pls. Ex. 3A). The license agreement was to remain in effect until the last of the specified patents had expired, subject to Brunswick's right to terminate after 5 and 10 years on 1 year's notice and at any time after February 19, 1975 (App. 353, Pls. Ex. 3, § 2.5).

annual extensions thereafter until February 19, 1974. The agreement provided that SCIC would employ Sheridan as its "head," "subject to the authority and jurisdiction" of a division of Brunswick "or for such other duties as the parties may hereafter agree upon" (see App. 372, Pls. Ex. 5, ¶ 1). Each party was given the right to terminate any time after the first 5 years on 6 months' notice (App. 372, Pls. Ex. 5, ¶ 2). The employment agreement contained a restrictive covenant which provided that Sheridan was not to engage in any activity "directly or through any other corporation" in competition with Brunswick during the period of his employment and for 5 years after February 19, 1974, if the agreement was not terminated sooner by Brunswick or SCIC (App. 374, Pls. Ex. 5, ¶ 7); if Sheridan terminated the Agreement, he was not to enter into any business "in competition with" Brunswick so long as any patent which he had licensed to Brunswick remained in effect (App. 375, Pls. Ex. 5, ¶ 10). If Brunswick or SCIC terminated the agreement before February 19, 1974 Sheridan was free to compete with Brunswick (App. 375, Pls. Ex. 5, ¶ 9).

Sheridan's compensation under the employment agreement was an annual salary of no less than $22,500.00 plus certain stock options. Under the license agreement Sheridan was to receive royalties on the sales of *all* products made by SCIC whether covered by his patents or not, so long as he remained in the employ of Brunswick or SCIC; if the employment agreement was terminated, Sheridan would receive royalties on sales of products covered by the licensed patents only (App. 355, Pls. Ex. 3, § 3.1). The agreement further provided that Sheridan would receive a minimum annual royalty of $20,000.00 during each of the first 5 years (App. 356, Pls. Ex. 3, § 3.2).

Shortly after the three agreements were executed, Brunswick constructed a large modern production facility at North Argyle for SCIC, and the business grew dramatically. Sheridan's royalties (disregarding the minimum) increased from about $12,000.00 in 1960 to $117,000.00 in 1967 (see App. 506, Pls. Ex. 34, Count I, ¶ 7 and Count IV, ¶ 4); by 1975 Sheridan's annual

royalties had reached $500,000 (App. 270-271, Tr. 1712-1713), and the total royalties paid to him had exceeded $2.8 million (App. 270, Tr. 1712). In late 1966 SCIC was merged into Brunswick. In about December, 1967 Brunswick formed Sherwood to take over the business of Brunswick's Health and Science Division. At the same time Brunswick transferred the North Argyle plant and the employment and license agreements with Sheridan to Sherwood.[4]

In 1963 Brunswick came on the market with what is now Sherwood's conductive tubing. The patent application for the Sherwood tubing was filed shortly after Brunswick acquired SCIC, and the patent issued to Sheridan in 1962 (App. 367, Pls. Ex. 3A). Annual sales of the conductive tubing increased from $50,000 in 1963 to $1.5 million in 1969 and $3.1 million by 1971 (App. 125-129, Tr. 610-614).

In October, 1967 Sheridan left Brunswick after receiving a letter from Willman advising him that his principal responsibility was "to spearhead product development" and not to supervise the North Argyle business (App. 531, Defs. Ex. R). In fact, Willman's letter did no more than state in writing what had been true in actual practice for a number of years (See App. 69, 76-79, Tr. 175, 254-257). Nevertheless, Sheridan rebuffed Brunswick's efforts to get him to return to work (App. 52, 243-244, Tr. 101, 1663-1664) and promptly set up his own company, National Catheter.[5] He built a virtual mirror image of the Sherwood plant only 30 feet away, and began making and selling specialized medical tubing in competition with Sherwood (See App. 55-57, 248-270, Tr. 114-116, 1686-1708).

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4. For the next two years Sherwood was a wholly-owned subsidiary; it then went approximately 15% public. It became a wholly-owned subsidiary of Brunswick once again on November 30, 1976.

5. In 1974 National Catheter was acquired by Mallinckrodt Corporation of St. Louis, Missouri for $22 million, $21 million of which went to Sheridan and his family (App. 273-275, Tr. 1725-1727).

Brunswick and Sherwood claimed that by his leaving Sheridan had terminated the employment agreement and was therefore precluded from competing with Sherwood by the noncompete provision contained in the 1960 employment agreement (App. 373, Pls. Ex. 5, ¶¶ 7, 9, 10). In early 1968 Brunswick and Sherwood filed suit against Sheridan and his company, asking for a declaration as to the meaning and legality of the provision and for its enforcement (App. 494, Pls. Ex. 33).[6]

Sheridan filed a counterclaim alleging that Brunswick had breached the employment agreement by relegating him to an "inferior position in the company." He also claimed that Brunswick had thereby forfeited its rights under the license agreement. His counterclaim sought damages for the alleged breach and an order rescinding the license agreement (See App. 506, Pls. Ex. 34; see also Appellants' Br. text at note 3).

The May, 1971 Settlement and the Instant Litigation

The parties disposed of the 1968 lawsuit after three years of discovery and negotiations by executing a written settlement agreement dated May 28, 1971 (App. 387, Pls. Ex. 9). The settlement provided, among other things not pertinent here, that the license agreement would remain in effect (¶¶ 2, 11), that Sherwood would pay Sheridan $100,000.00 (¶ 11) and that Sheridan and his company would be free to compete generally with Sherwood, subject only to the narrow restrictions set forth in paragraph 5:

> "5. For a period of five years from the date hereof, neither Sheridan nor National Catheter shall, directly or indirectly, whether as owner, employee, officer, director, advisor or in any other capacity, do any of the following, nor assist or enable (whether by sale of an invention or otherwise) any person, corporation or other business entity to do any of the following:

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6. Because it was a party to the employment agreement, Brunswick was joined as a plaintiff in the 1968 lawsuit.

(a) manufacture, or have manufactured, disposable needles, metal cannulae or hypodermic syringes and component parts hereof; or

(b) manufacture, have manufactured, use, sell or otherwise deal in flexible tubing made by any process in which the wall thickness of the tubing or the inner and/or outer diameters of the tubing is/are controlled so as to incorporate the features or configuration of an integral bubble or funnel similar to those manufactured by Sherwood as of February 1969,[7] *or incorporating features or configuration of an x-ray[8] or conductive line similar to the products manufactured by Sherwood as of February 1969.*"

(We have underscored the specific language in dispute in this case.)

Three days before the settlement agreement was signed, a patent on the "conductive line" tubing now produced by National Catheter was issued to Isaac Jackson, who had formerly been employed by Brunswick at the North Argyle plant. Jackson left Brunswick in late 1967 and went to work for Sheridan's company, National Catheter, shortly thereafter (App. 158-159, 191, Tr. 1056-1057, 1132). During the settlement negotiations Sheridan and Jackson were aware that this "conductive line" tubing patent was pending, and the evidence indicates that Sheridan did not agree to sign the settlement agreement until

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7. This language was invoked by Sherwood in an amendment to the complaint in this case in the belief that it applied to a catheter used in open heart surgery (known as a vena cava cannula) which National Catheter was producing. After Sheridan advised Sherwood that the provision was inapplicable, Sherwood undertook limited discovery on this issue, satisfied itself that Sheridan's assertion was correct, and dropped the claim. This incident, which was not proved to have damaged Sheridan in any way, hardly supports the claim in appellants' brief (Summary of Argument, text at notes 11 and 12) that it proves that Sherwood was acting with anti-competitive motives, or with any purpose except to enforce the agreement between the parties.

8. An x-ray line is the same thing as a conductive line, except that rather than being electrically conductive the line is radio opaque, that is, visible upon x-ray. Tubing containing an x-ray line is not involved in this litigation.

he knew that the patent had issued (App. 271-272, Tr. 1717-1718). At the time it executed the agreement, however, Sherwood did not know of either the patent application or its issuance (App. 272, Tr. 1718). Shortly after the settlement agreement had been signed Sheridan commenced efforts to produce "conductive line" tubing under the Jackson patent.

In December, 1971 and again in April, 1972 American Hospital Supply Corporation, the nation's largest medical supply organization, ordered quantities of "conductive line" tubing from National Catheter. In April, 1972, upon learning that American Hospital Supply was contemplating the purchase of "conductive line" tubing from Sheridan's company, Willman (then Sherwood's president) contacted American Hospital Supply and informed it that it was Sherwood's belief that a sale of the National Catheter tubing to American Hospital Supply would be in violation of the settlement agreement and that Sherwood intended to defend itself against this violation. Willman also provided American Hospital Supply with a copy of the settlement agreement and a sample of Sherwood's conductive tubing so that it could judge for itself whether Sheridan was violating the agreement. By no later than June 27, 1972 American Hospital Supply had resolved the matter to its own satisfaction and had advised National Catheter that it would go ahead with its intended purchase of the tubing. Subsequently, National Catheter produced the tubing and in about December, 1972 delivered it to American Hospital Supply. Thereafter additional sales of the tubing were made to American Hospital Supply and others. (App. 585, 588, Defs. Ex. BX and BY; App. 393, 394, Pls. Exs. 12 and 13; App. 61-63, 65-67, 71, 74, 220-222, 224, 245-247, Tr. 131-133, 135-137, 223, 244, 1471, 1476, 1479-1482, 1498, 1671-1672.)[9]

Sheridan asserts that as a result of Willman's communications with American Hospital Supply, National Catheter lost over $750,000 in sales (Br. text following note 8). The un-

9. The American Hospital Supply incident is described in greater detail below at pages 19-20.

disputed evidence demonstrates, however, that American Hospital Supply purchased exactly what it had ordered. The long delay was attributable to National Catheter's inability or refusal to complete production of the tubing until December, 1972 (App. 233-238, 2[illegible]5, Tr. 1624-1629, 1670).

Sherwood filed this suit in July, 1972 charging that the National Catheter "conductive line" tubing was "flexible tubing" "incorporating features or configuration of [a] conductive line similar to the [conductive tubing] manufactured by Sherwood as of February 1969" (App. 389, Pls. Ex. 9, ¶ 5(b)). Sheridan denied this charge and filed a counterclaim. In Count I of his counterclaim (the only part of the case which is before this Court), Sheridan alleged that Brunswick and Sherwood "have combined and conspired to misuse Paragraph 5 [of the settlement agreement] to prevent defendants from competing with [them] in the manufacture and sale of medical tubing" (¶ 9), that Brunswick and Sherwood "have combined and conspired to institute the instant action" (¶ 10), and that Brunswick and Sherwood "have also combined and conspired" to threaten, coerce, persuade or attempt to persuade a number of third parties not to do business with Sheridan (¶ 11)—all in violation of Section 1 of the Sherman Act. In Count I Sheridan also alleged that Brunswick and Sherwood have engaged in a "combination and conspiracy . . . to attempt to monopolize the development, manufacture and sale of catheters and medical tubing in the United States" in violation of Section 2 of the Sherman Act (¶ 13).

As we will show, the District Court properly directed a verdict because Sheridan failed to present evidence showing any violation of Sections 1 or 2 of the Sherman Act.

ARGUMENT

I.

THE DIRECTED VERDICT WAS PROPERLY GRANTED AS TO SECTION 1 OF THE SHERMAN ACT BECAUSE SHERIDAN FAILED TO OFFER EVIDENCE OF ANY CONTRACT, COMBINATION OR CONSPIRACY TO RESTRAIN TRADE

In order to get to the jury under Section 1 of the Sherman Act, Sheridan had to offer evidence which made out a prima facie showing that either Sherwood or Brunswick had entered into a "contract, combination . . . or conspiracy, in restraint of trade" and that Sheridan suffered injury as a result.

All of the cases of which we are aware, including cases decided in this Circuit and in the United States Supreme Court, and all of the respected authorities who discuss Section 1 of the Sherman Act, agree that in order to satisfy the "contract, combination or conspiracy" requirement of the statute the complaining party must prove the existence of "a unity of purpose or a common design" among two or more persons[10] to restrain trade. *Kiefer-Stewart Co.* v. *Joseph E. Seagram & Sons, Inc.*, 340 U. S. 211, 213 (1951).

Citing numerous cases from all Circuits, J. Von Kalinowski, 1 *Antitrust Laws and Trade Regulations* § 6.01[1] at 6-5 (1969), states:

> "The technical differentiation of contract, combination, and conspiracy is, however, of little moment in an analysis of Section 1. What is of essential importance in this connection is the existence of those two factors which are common to the concepts of contract, combination, and conspiracy:
>
> (1) a plurality of actors, that is, two or more persons; and
>
> (2) concerted action."

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10. "Persons" in this context includes, of course, corporations and other business entities.

The cases are in full accord:

> "Section 1 of the Sherman Act proscribing every 'contract, combination, or conspiracy' in restraint of trade is directed only at joint action. Fundamental, then to any section 1 violation is the finding of an agreement between two or more parties. . . ." *Ford Motor Co.* v. *Webster's Auto Stales, Inc.*, 361 F. 2d 874, 878 (1st Cir. 1966).
>
> "It is not necessary that there be a formal agreement between the conspirators. If the evidence satisfies the jury that they acted in concert, understandingly and with the design to consummate an unlawful purpose, it is sufficient. . . ." *Lawlor* v. *Loewe*, 209 Fed. 721, 725 (2d Cir. 1913).

See also Turner, *The Definition of Agreement Under the Sherman Act: Conscious Parallelism and Refusals to Deal,* 75 Harv. L. Rev. 655, 655-656 (1962):

> "The Congress which wrote the Sherman Act directed its main thrust against business conduct involving two or more parties. Section 1, proscribing every 'contract, combination or conspiracy' in restraint of trade, is strictly confined to joint action. . . . For most kinds of anticompetitive business conduct, condemnation has depended and continues to depend on finding two or more parties who may be said to have 'agreed' to do what was done, since 'agreement' is an essential ingredient of 'contract, combination or conspiracy.' "

The cases and authorities set forth above clearly show that Sheridan was required to present evidence of an agreement or joint activity between or among two or more persons, each of whom shared the common design and unity of purpose unreasonably to restrain trade. The District Court directed a verdict as to Section 1 of the Sherman Act because Sheridan utterly failed to present evidence of any such agreement or joint activity.

The only acts upon which appellants rely to show joint activity are the settlement agreement itself, the institution of this lawsuit, and Willman's notification to American Hospital Supply of the terms of the settlement and of appellees' intention to enforce it. As will appear (*infra,* pp. 19-20), the latter episode consisted entirely of two telephone calls and accompanying

letters on the same day from the president of Sherwood, so that on no theory can it be regarded as the conduct of two parties[11] —unless everything done by a subsidiary is to be treated as the conduct of the parent and, therefore, as proof without more of a conspiracy between them, which would be absurd. This leaves the settlement agreement and the lawsuit. As to the former, appellants have never pointed to any evidence, in the court below or in their brief here, which even showed who the parties to the allegedly unlawful joint conduct were supposed to be: Was it appellees or either of them and Sheridan? Or was it just the two appellees, Brunswick and Sherwood? We shall show that on neither theory would the facts warrant a finding that there was a joint undertaking or agreement unreasonably to restrain trade.

During the argument on Brunswick's motion for a directed verdict, the District Court repeatedly asked counsel for Sheridan to point to the evidence showing the combination or conspiracy upon which Sheridan relied, and Sheridan's counsel was repeatedly unable to do so:

> "THE COURT: What evidence do you have in this regard that there was an anti-trust conspiracy and a monopoly design?" (App. 285, Tr. 2111).

After some discussion of the law by Sheridan's counsel, the District Court again interrupted and said:

> "THE COURT: Where is the combination? That is what I can't find." (App. 287, Tr. 2113.)

After even further legal discussion by counsel, the District Court again asked:

> "THE COURT: Where did the evidence come that they combined, and conspired, no matter who he worked for, to impose an unreasonable restraint on trade in this particular article?" (App. 289, Tr. 2115.)

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11. At one stage of the litigation, appellants' counsel suggested that the incident proved a conspiracy between Sherwood and American Hospital Supply. But there was no showing of any agreement between them at all. Indeed, after a short delay to consult counsel, American Hospital Supply refused to do what Willman obviously wanted.

After yet further argument by Sheridan's counsel on matters extraneous to the court's inquiries, the District Court finally interrupted and said:

"THE COURT: . . . I am looking for the evidence that supports your counter claim. I am honest enough to say that I reviewed it carefully, and I was surprised that I count six witnesses on each side, live witnesses, and we had depositions and arguments, and I don't know why it took so long either, after I counted the six witnesses.

"I have seen the testimony, and I have the yellow sheets to prove it.

"I don't find evidence here.

"MR. ARNES: Well, here is the evidence. There is a contract—

"THE COURT: We can have a look at the legal theories and the allegation, and the case law, but we need evidence here." (App. 302, Tr. 2128.)

The foregoing repeated requests for evidence, rather than legal theories and rhetoric, went unanswered by Sheridan's counsel.

As a result, Judge Foley concluded in granting the motion for a directed verdict:

"But I have reviewed the evidence carefully, and I am a Judge that always looks for evidence to support allegations. Otherwise I am not satisfied.

"But usually when I have a jury, and it has always been my custom, and rarely have I ever directed a verdict and taken certain issues away from a jury, and that comes from the experience of knowing that the Court of Appeals, Second Circuit, Judge Frank years ago cautioned to get a complete trial, and then set aside.

"But my conviction is firm, and it is strong that to withhold a decision at this time, and at this stage of the trial by a jury, in the exercise of caution, would be unjustified, and unfair to the Plaintiff, and contrary to the interests of justice, and contrary also to the firm conviction that I have in my mind that three counts of this counter claim have not been proven to the extent that they should stand, and that the motion for a directed verdict should be granted in this regard." (App. 315, Tr. 2152.)

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"I find no evidence in this record of a conspiracy, and they are serious charges, or a combination, to prove a monopoly in regard to the allegations made in that respect in the claims of the anti-trust, Count one. There is no evidence, apparent to me, to support the serious charge of conspiracy to violate the anti-trust statute, and that most, I think, there is a dispute among lawyers, as we have tried their case, but the meaning of words in that type of dispute is common to our system of law. At the most, I find in the evidence isolated incidents in which never could be drawn, in my judgment, the conclusion that there was a deliberate attempt to monopolize, or to unreasonably restrain trade." (App. 319, Tr. 2156.)

The District Court's inquiry remains unanswered in appellants' brief in this Court. The reason is that the evidence needed to support a contention that either Brunswick or Sherwood entered into a "contract, combination or conspiracy" simply does not exist.

A. The Settlement Agreement

1. The Settlement Did Not Constitute Unlawful Joint Action Between Brunswick and Sherwood

Any contention that the fact that Brunswick and Sherwood both signed the settlement agreement constituted the necessary joint or conspiratorial conduct is supportable neither in fact nor in law.

The 1968 complaint named both Brunswick and its successor Sherwood as parties plaintiff. Inasmuch as both were parties to the prior lawsuit, both were necessary parties to the settlement of it in 1971. The settlement agreement imposed obligations on both Brunswick and Sherwood. For the contractual obligations to be binding, it was obviously necessary for each to sign the settlement agreement, and their doing so could hardly be said to constitute an unlawful conspiracy. Sheridan offered no evidence that, by signing the settlement agreement, Brunswick

and Sherwood undertook to restrain trade between themselves.[12] Nor is there a shred of evidence to support Sheridan's allegation that Brunswick and Sheridan got together and agreed to adopt an "improperly broad interpretation" of the May, 1971 settlement agreement (Appellants' Br. text at note 11).

2. The Settlement Did Not Constitute Unlawful Joint Action Between Sheridan and Appellees

The short answer to any contention that the required plurality of actors consisted of Sheridan and either or both of appellees is that Sheridan[13] has never pleaded or offered evi-

12. *Kiefer-Stewart Co.* v. *Joseph E. Seagram & Sons, Inc.*, 340 U. S. 211 (1951), and other cases holding that affiliated corporations may be the parties to a combination or conspiracy under Section 1 of the Sherman Act do not apply here for two reasons. First, as is shown above and in the text which follows, the record contains no evidence that Sherwood and Brunswick engaged in any joint activity in restraint of trade. Accordingly, we never reach the question, addressed by these cases, whether such joint activity could constitute a combination or conspiracy within the meaning of § 1. Second, even if there were evidence of joint activity by Sherwood and Brunswick in restraint of trade, the *Kiefer-Stewart* line of cases does not lead inexorably to the conclusion that this would constitute a combination or conspiracy under § 1. Indeed, quite the contrary is true. In *Kiefer-Stewart* the conspirators were two subsidiaries of Seagram which *competed with each other*. Sherwood and Brunswick do not and never have competed with each other. Sherwood is a subsidiary which was created simply to carry on business operations formerly carried on by a division of Brunswick. And, as this Court said in *Triebwasser & Katz* v. *American Telephone & Telegraph Co.*, 535 F. 2d 1356, 1358 n.1 (2d Cir. 1976), the *Kiefer-Stewart* doctrine does not "necessarily" extend to joint action of a parent "and its non-competing wholly-owned subsidiary." See also *Beckman* v. *Walter Kidde & Co.*, 316 F. Supp. 1321 (E. D. N. Y. 1970), *aff'd*, 451 F. 2d 593 (2d Cir. 1971), *cert. denied*, 408 U. S. 922 (1972).

13. National Catheter Corporation is not a separate entity from Sheridan for Sherman Act purposes in this context for the same reason that Brunswick and Sherwood are not separate entities. We therefore speak only of Sheridan.

dence in support of any such theory. And for good reason, for it has consistently been Sheridan's position that the settlement agreement did not extend to his "conductive line" tubing.

We recognize that a contract containing a restraint is not immune from scrutiny under the antitrust laws. *Cf. Newburger, Loeb & Co.* v. *Gross,* 1977-2 Trade Cases ¶ 61,604 (2d Cir. 1977). But to give rise to a claim for damages under Section 1 there must have been an agreement by which two parties have undertaken to restrain trade. Here, the undisputed evidence, offered by both Sheridan and Brunswick, was that Sheridan purposefully refused to refrain from dealing in "conductive line" tubing, that he (or his company) went ahead and dealt in it as though the agreement did not cover it, and that the company made substantial sales of that tubing[14] during the period covered by the lawsuit. Even Sheridan's counsel contended that Sheridan made no agreement to refrain from selling "conductive line" tubing. Speaking of the settlement agreement, Sheridan's counsel told Judge Foley that "Sheridan ignored it and he did fine" (App. 294, Tr. 2120), and Sheridan's position since the signing of the contract has consistently been that the agreement did not extend to his tubing.[15] Under these circumstances, the District

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14. The evidence showed that during the period January, 1972 through February, 1976 Sheridan's company sold \$2,865,164 worth of "conductive line" tubing at a gross profit margin of 58 percent, which yielded \$1,661,795 in gross profits (App. 520, Pls. Ex. 43).

15. Sheridan's position was required to avoid the application of the doctrine of *in pari delicto* because otherwise appellants would have agreed to a covenant they now claim is unlawful; despite what is said in appellants' brief (Br. Part II-A), nothing in the record suggests that appellees and Sheridan were not acting on an equal footing in agreeing to the 1971 settlement. This Court has suggested that a plaintiff who is equally responsible for the violation would be denied relief. *Bernstein* v. *Universal Pictures, Inc.,* 517 F. 2d 976, 982 (1975). The five Justices (White, Marshall, Fortas, Harlan and Stewart (392 U. S. at 142-156)) who wrote or expressed their views outside of the plurality opinion in *Perma Life Mufflers, Inc.* v. *International*

(Footnote continued on next page.)

Court correctly was unable to find any evidence that Sheridan participated in a "contract, combination or conspiracy" that restrained trade.

B. The Institution of the Lawsuit Did Not Constitute Unlawful Joint Action

As to the other alleged evidence of joint behavior by Brunswick and Sherwood, the filing of the instant lawsuit, the cases clearly show that such action does not constitute a "contract, combination or conspiracy" unreasonably to restrain trade. The submission of legal controversies to courts of law is *the* approved, and certainly *an* approved, method of resolving them.

> "The right of access to the courts is indeed but one aspect of the right of petition. . . .
>
> "We conclude that it would be destructive of rights of association and of petition to hold that groups with common interests may not, without violating the antitrust laws, use the channels and procedures of state and federal agencies and courts to advocate their causes and points of view respecting resolution of their business and economic interests vis-a-vis their competitors." *California Motor Transport Co.* v. *Trucking Unlimited,* 404 U. S. 508, 510-511 (1972).

Except in unusual circumstances, such as persistent harassment, "repetitive, sham litigation," *Vendo Co.* v. *Lektro-Vend Corp.*, 97 S. Ct. 2881, 2889 n.6, 53 L. Ed. 2d 1009, 1019 n.6, 1025 (1977), or a "a pattern of baseless, repetitive claims," *id.* at 1020 n.6, *California Motor Transport Co.* v. *Trucking Unlimited,* 404 U. S. 508, 513 (1972), the bringing of a lawsuit is not unlawful, and the fact that two parties join in a single complaint does not convert it into a conspiracy or combination. Sheridan presented no evidence, and the District Court found

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(Footnote continued from preceding page.)

Parts Corp., 392 U. S. 134 (1968), supported the availability of an *in pari delicto* defense where the parties were operating on an equal footing, with one not dominant or coerced by the other. Of the plurality of four, only Mr. Justice Brennan is now on the Court.

none, which would support a conclusion that Brunswick and Sherwood knowingly and in bad faith filed a suit with no merit to restrain Sheridan from dealing in "conductive line" tubing.

C. The American Hospital Supply Incident Was Not Evidence of Unlawful Joint Action

The only other evidence relied upon by appellants relates to the American Hospital Supply incident, in which Willman, Sherwood's president, called American Hospital Supply, told them that he had heard that Sheridan was about to sell "conductive line" tubing, that this would be in violation of the settlement agreement, and that Sherwood intended to protect itself from what he regarded as this breach of contract. Sheridan offered no evidence to show that Willman's acts were the result of any agreement or joint undertaking between Sherwood and Brunswick. The undisputed facts surrounding this incident are as follows:

1. On December 1, 1971 American Hospital Supply ordered $43,954 worth of "conductive line" tubing from Sheridan's company (App. 585, Def. Ex. BX) and on April 18, 1972, an additional quantity of the same tubing for $62,770 (App. 588, Def. Ex. BY).

2. In April, 1972, John Willman, Sherwood's president and the person who had signed the May 28, 1971 settlement agreement on behalf of Sherwood, learned of Sheridan's intended sale of tubing to American Hospital Supply Corporation and believed that Sheridan's dealing in such tubing was a violation of the settlement agreement (App. 71, Tr. 223).

3. On April 27, 1972, Mr. Willman telephoned American Hospital Supply, talked to a Mr. Schmidt whom Willman had long known, and also about the same time talked to an American Hospital Supply purchasing agent, Mr. Grossman (App. 65-67, Tr. 135-137), and told them as follows (App. 61-63, Tr. 131-133):

> "Well, to the best of my recollection, I told him that it was my understanding that American was contemplating

> the purchase or was purchasing a form of conductive tubing from Mr. Sheridan that was in violation of our agreement with him that he would not produce such a tube. . . . and that it was going to be necessary for us to defend ourselves against this violation, and that was the end of it beyond Mr. Schmidt's request that I send him a copy of the settlement agreement so his counsel could examine it."

His object was "to let American Hospital Supply know if they were indeed about to do it that they were buying something or contemplating buying something that might get them, through inadvertence on their part, involved as a co-defendant with Dave Sheridan in a lawsuit that we were going to prosecute" (App. 74, Tr. 244).

4. Late on the same day, Willman sent Schmidt two letters, one enclosing "a sample of our conductive line tubing, so that you will be able to understand our contention that it is 'similar' to the one Sheridan is producing" (App. 393, Pls. Ex. 12). The other letter (App. 394, Pls. Ex. 13) enclosed "a copy of our Settlement Agreement of May 1971," and concluded: "After your counsel has had a chance to review it, I will appreciate hearing from you."

5. On the following day, April 28, 1972, American Hospital Supply telephoned Sheridan's company and told the latter to hold up on the purchase orders (App. 220, Tr. 1471). On May 11, 1972, approximately two weeks later, American Hospital Supply contacted Sheridan's company and said "O. K., full speed ahead" (App. 221, Tr. 1479-1480), in the expectation that Sheridan's company would indemnify it if it became involved in a lawsuit between Brunswick and Sheridan. However, Sheridan refused to provide an indemnity agreement (App. 246-247, Tr. 1671-72). On June 26, 1972, American Hospital Supply's general counsel, Richard Hull, advised American Hospital Supply's purchasing department that it was "O. K. to proceed" even without an indemnity agreement (App. 221, 224, Tr. 1476, 1498). Sheridan's company was informed of this decision toward the end of June, 1972 (App. 222, Tr. 1481-1482).

There was no evidence of any communications between Sherwood and Brunswick or between them and American Hospital Supply on the subject except for the phone calls and letters of April 27.

The foregoing facts constitute the entirety of the so-called "American Hospital Supply" incident.

It was doubtless with this in mind that Judge Foley stated that "[a]t the most, I find in the evidence isolated incidents in which never could be drawn, in my judgment, the conclusion that there was a deliberate attempt to monopolize, or to unreasonably restrain trade." (App. 319, Tr. 2156).

The record fully supports Judge Foley's conclusion. Sheridan offered no evidence, and the record contains none, that Willman contacted American Hospital Supply pursuant to some "contract, combination or conspiracy" of any kind with Brunswick.

Furthermore, the cases and authorities uniformly hold that one party to a contract is privileged to do exactly what Willman did. Restatement of Torts, § 773 at 87 (1939), states:

> "One is privileged purposely to cause another not to perform a contract, or enter into or continue a business relation, with a third person by in good faith *asserting or threatening to protect properly* a legally protected interest of his own which he believes may otherwise be impaired or destroyed by the performance of the contract or transaction." (Emphasis supplied.)[16]

The Restatement's rule endorses what appears to be the leading New York case dealing with this privilege, *Knapp* v. *Penfield*, 143 Misc. 132, 256 N. Y. S. 41 (Sup. Ct. 1932). *Knapp* is quoted approvingly in *Belsen* v. *Sol Cafe Mfg. Corp.*, 24 N. Y. 2d 682, 687, 301 N. Y. S. 2d 610, 613, 249 N. E. 2d 459, 461 (1969), and *Hendler* v. *Cuneo Eastern Press, Inc.*, 279 F. 2d 181, 184-85 (2d Cir. 1960). In the *Knapp* case, the court stated:

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16. The Restatement (Second) of Torts contemplates no substantive change. See Restatement (Second) of Torts, § 773 at 55 (Tent. Draft No. 23, April, 1977).

> "Procuring the breach of a contract in the exercise of an equal or superior right is acting with just cause or excuse, and is justification for what would otherwise be an actionable wrong . . . Persons acting for the protection of contract rights of their own which are of an equal or superior interest to another's contractual rights may invade the latter with impunity." 143 Misc. at 134-35, 256 N. Y. S. at 44.

This rule applies whether a party wins or loses his case on the merits. All that the law requires is that he honestly believe that his legal rights would be violated by the other's conduct. See Restatement of Torts, § 773 (quoted above), Illustration 1; *Kaplan* v. *Helenhart Novelty Corp.*, 182 F. 2d 311 (2d Cir. 1950) (applying New York law), where the court stated:

> "* * * [I]t is not an actionable wrong for one in good faith to make plain to whomsoever he will that it is his purpose to insist upon what he believes to be his legal rights, even though he may misconceive what those rights are." 182 F. 2d at 314.

Accord *Hendler* v. *Cuneo Eastern Press, Inc.*, 279 F. 2d 181 (2d Cir. 1960) (contract rights); *Eastern States Petroleum Co.* v. *Asiatic Petroleum Corp.*, 103 F. 2d 315 (2d Cir. 1939) (property rights). See also *Dinkins* v. *General Aniline & Film Corp.*, 214 F. Supp. 276, 280-281 (S. D. N. Y. 1962).

On the record, it is indisputable that Sherwood honestly believed that defendants' proposed sale to American Hospital Supply would violate its contract rights. This appears not only from Willman's uncontradicted testimony (App. 80-81, Tr. 264) but also from the fact that he provided American Hospital Supply with a copy of the settlement agreement (App. 394, Pls. Ex. 13) and a sample of Sherwood's tubing (App. 393, Pls. Ex. 12), and urged that they be submitted to counsel for consideration. These are not the actions of one who believes that his claims have no merit.

Moreover, Sheridan failed to offer evidence, and the record contains none, that the actions of Willman generated any restraint of trade, unreasonable or otherwise. Surely the two-month period of time (from late April, 1972 to late June, 1972), during which

American Hospital Supply tried to obtain an indemnity agreement from Sheridan and then, failing that, satisfied itself of its legal position, could not be characterized as an "unreasonable restraint of trade" devised by Willman.

For the above reasons, Sheridan offered no evidence of any "contract, combination or conspiracy" to restrain trade, as those terms are used in Section 1 of the Sherman Act. As a result, the District Court was clearly correct in directing a verdict against Sheridan with respect to the latter's Section 1 theory.

II.

THE DIRECTED VERDICT WAS PROPERLY GRANTED AS TO SECTION 2 OF THE SHERMAN ACT BECAUSE SHERIDAN FAILED TO OFFER EVIDENCE OF THE ELEMENTS NECESSARY TO MAKE OUT A CASE OF MONOPOLIZATION OR ATTEMPTED MONOPOLIZATION

Sheridan's theory under Section 2 of the Sherman Act is not clear. Defendants' Amended Complaint, at paragraph 13, charges a "combination and conspiracy . . . to attempt to monopolize the development, manufacture and sale of catheters and medical tubing." Nothing is said about actual monopolization, which is, of course, a distinct offense under the Sherman Act. Yet Section V of appellants' brief claims "monopolization," "attempt to monopolize," and "combining or conspiring to monopolize."

We will discuss the record both in the context of a "monopolization" theory and an "attempt to monopolize" theory; the claimed theory of "combining or conspiring to monopolize" will be disposed of by our discussion of those two issues, and also by the argument under Point I, *supra,* which demonstrates that there was no evidence of any conspiracy.

It is axiomatic that "[i]n order to fall within § 2, the monopolist must have both the power to monopolize, and the intent to monopolize," the relevant market. *Kreager* v. *General Electric Co.,* 497 F. 2d 468, 471 (2d Cir.), *cert. denied,* 419 U. S. 861 (1974). "Monopoly power" is traditionally defined as the power

"to control prices or exclude competition" in a relevant market. *United States* v. *E. I. DuPont de Nemours & Co.*, 351 U. S. 377, 391 (1965) (*Cellophane*). Stated differently, monopoly power is the power to set one's own price "substantially immune from competitive forces," *ABA Antitrust Civil Jury Instructions* 98 (1972), citing *Utah Pie* v. *Continental Baking Co.*, 349 F. 2d 122 (10th Cir. 1965), *rev'd on other grounds*, 386 U. S. 685 (1967).

In order to set up a theory of attempted monopolization under the Sherman Act it was incumbent upon Sheridan to offer evidence from which each of the following elements could have been inferred:

(i) That Brunswick or Sherwood had the specific intent to monopolize a relevant market;

(ii) That Brunswick or Sherwood engaged in some predatory or otherwise unfair act in furtherance of such specific intent;

(iii) That Brunswick's or Sherwood's act (or acts) or course of conduct created a dangerous probability that plaintiffs would succeed in monopolizing the relevant market; and

(iv) That defendants were damaged in their business or property as a proximate result thereof.

American Tobacco Co. v. *United States*, 328 U. S. 781, 785 (1946); *United States* v. *Chas. Pfizer & Co.*, 245 F. Supp. 737, 738-739 (E. D. N. Y. 1965).

In their brief appellants do not explain how Sheridan's evidence would, even if believed by the jury, prove either a claim of monopolization or of attempted monopolization. Sheridan's position appears to be simply that (1) prior to 1972 Sherwood was the only firm that sold clear plastic tubing with a black line running along its length ("conductive line" tubing); and (2) that by attempting to enforce the May 28, 1971 settlement agreement (by filing this lawsuit and by contacting American Hospital Supply) Sherwood or Brunswick attempted to maintain or extend that position. None of the cases cited in the appellants' brief and

none of the cases of which we are aware hold that such facts, without more, justify submitting a Section 2 Sherman Act claim to the jury.

Whenever an innovator devises a new product and places it on the market there necessarily will be a time during which the innovator is the sole supplier of that product. Similarly, whenever a businessman brings a unique business service into a geographical area where the service was previously unavailable he becomes the sole provider of that service for a period of time. Either the innovator or the new businessman may be said to have 100 percent of some "relevant market," both in the product sense and in the geographic sense. Suppose that a new concern begins competing with the original innovator by a means which ordinarily would give rise to a remedy in the courts, such as by stealing trade secrets, or by inducing customers to break their contracts with the innovator. Shall the latter be barred from judicial relief against the wrongdoing new competitor because such relief might restore him to his original position as the sole supplier in the relevant market? Clearly not. Similarly a company which is lawfully the only producer of a product and which contracts to sell a quantity of it to a buyer is entitled, without violating the antitrust laws, to sue to prevent the buyer from breaching his contract to purchase even if the necessary effect might be to prevent someone else from making the sale, thus leaving the seller as the sole producer.

The Supreme Court in *American Tobacco Co.* v. *United States, supra,* has indicated that even where the original entrant into a field may be said to have a monopoly, and the intent to use it, such facts, standing alone, may not be enough to impose liability under Section 2:

> "The present cases are not comparable to cases where the parties, for example, merely have made a new discovery or an original entry into a new field and unexpectedly or unavoidably have found themselves enjoying a monopoly coupled with power and intent to maintain it. . . ." 328 U. S. at 786.

The record here discloses no effort by Sherwood to do more than to seek to enforce its contract rights against a single person.[17] But the ". . . exclusion of a single person from competition is not monopoly. The essence of monopoly is power to effect the exclusion of competition generally in a field for the benefit of a particular person or class," *Interborough News Co.* v. *Curtis Publishing Co.*, 127 F. Supp. 286, 298 (S. D. N. Y. 1954), *aff'd*, 225 F. 2d 289 (2d Cir. 1955). Any other rule would make it impossible for the product innovator or the creative businessman to preserve his contract rights without incurring the risk of treble damage liability or violation of a federal criminal statute.

Here, as we shall demonstrate, there is no evidence that appellees possessed monopoly power. Although Sheridan offered no evidence from which a relevant market could be intelligently defined, let it be assumed for these purposes that the relevant market is clear plastic tubing with a conductive line running along its length for use in the operating room ("conductive line" tubing). The evidence showed that, notwithstanding Sherwood's single protestation, based upon what it thought were its contract rights, American Hospital Supply went into the market and sold National Catheter's "conductive line" tubing in competition with Sherwood (App. 520, Pls. Ex. 43).

In addition, in 1974 the Davol Company came on the market with a substantially identical and directly competing product, *i.e.*, clear plastic tubing with a conductive line running along its length for use in the operating room; during Davol's first full year of sales, it captured 10.6 percent of this market (App. 129-130, Tr. 621-22). Since then, yet another competitor, Bard, has entered the market with the same type of tubing (App. 154, Tr. 971). The record contains no evidence whatsoever from which one could infer any attempt by Sherwood to fore-

17. Appellants point out that appellees are seeking to enforce the covenant against Jackson's patent as well as Sheridan's. But, as we note below (see p. 48, *infra*), if Jackson had not tied himself to Sheridan's corporation, he would have been free to exploit his patent.

close Davol's or Bard's entry into the market or to interfere with their sales activities.

Moreover, Sheridan offered no evidence of any barriers to entry into the market. The American Hospital Supply, Bard, and Davol competition would appear conclusively to establish that, even though Brunswick had an exclusive license to Sheridan's 1962 patent, there were no barriers to entry. It is obvious that the lack of significant barriers to entry must preclude any firm from achieving and exercising monopoly power.

Sheridan was also unable to present a shred of evidence that Sherwood sought to place itself in the position of controlling price in any relevant market. The record contains no evidence of any analysis of Sherwood's pricing practices with respect to the tubing here under discussion and contains no evidence pertaining to the prices at which others were selling such tubing.

Nor did Sheridan attempt to compare the price of clear conductive tubing with the price of opaque conductive tubing, which had been used for the same purpose for about 30 years prior to the appearance of "conductive line" tubing on the market (App. 31-32, Tr. 66-67). Any analysis of price behavior with respect to the tubing which Sheridan contends constitutes the relevant market would necessarily have to include an analysis of how fluctuations in the price of "conductive line" tubing affect the demand for the opaque tubing, for cross-elasticity of demand is a fundamental inquiry where concepts of pricing behavior are at issue. *Cellophane, supra,* 351 U. S. at 400.

What has been said above disposes of any contention that there was evidence to submit to the jury on the question of "monopolization." With reference to the elements of attempted monopoly (see p. 24, *supra*), Sheridan's evidence presented nothing from which one could infer either a specific intent to monopolize or a dangerous probability of success.

Appellants' brief points to no testimony or exhibits from which the jury might conclude that Sherwood specifically in-

tended to eliminate competition generally in the market for "conductive line" tubing or in any other market. The brief simply sets forth the bald conclusion that "Brunswick's conscious and willful acquisition of market power plus its deliberate attempts to exclude new entrants are the unmistakable earmarks of an unlawful scheme to attempt to monopolize" (Br. Part V). No transcript or other reference is cited to support this conclusion. This is merely appellants' exaggerated characterization of the covenants not to compete between Brunswick and Sheridan and of Brunswick's attempts to enforce such covenants.

With respect to any facts showing a dangerous probability of success of Sherwood's monopolizing, appellants' brief is silent, as it must be in light of the complete lack of evidence of any such probability. Indeed, the entry into the market by Davol and Bard and the competitive sales activity of American Hospital Supply Corporation make it impossible for Sheridan to show that at any time there was a dangerous probability that Sherwood would achieve the power to control price or exclude competition. Under such circumstances a case should be dismissed without being submitted to the jury:

> ". . . [Plaintiff] failed to offer any proof defining the relevant market. It failed to prove that any of the corporate defendants had the requisite monopoly power or any intent to monopolize, coupled with a 'dangerous probability' of success. [Citations omitted.] Since there was a total failure of proof on the Section 2 claims, they were properly dismissed without submission to the jury. . . ." *Kreager* v. *General Electric Co.*, 497 F. 2d 468, 471 (2d Cir.), *cert. denied,* 419 U. S. 861 (1974).

Appellants' brief suggests, without so stating, that the record contains "evidence of conduct including the extraction of broad noncompete covenants and litigation and threats of litigation based on those covenants" and "[t]ortious threats to potential customers of involvement in litigation" (Br. Part V). Appellants do not cite the record to support these allegations, for no support exists.

The alleged "extraction of broad noncompete covenants" presumably is intended to refer to the covenants in the 1960 agreement and the 1971 settlement. The latter was merely the settlement of a contested lawsuit as to the effect and legality of the former. The brief does not explain the source of the conclusion that such covenants were "extracted" or that they represented a part of a course of conduct looking toward the elimination of competition in connection with the tubing here in question. Presumably, Sheridan is likening the noncompete provision of the May 28, 1971 settlement agreement to the adhesion-type noncompete agreements in which some firms take advantage of the employer-employee relationship to forestall competition through the use of unnecessarily broad noncompete clauses in employment contracts. But the covenant here was ancillary not only to Sheridan's employment but also to the sale of his business to Brunswick. Moreover, this case certainly does not present the disparity of bargaining power which one finds in typical employer-employee cases: by the time the settlement agreement was signed, Sheridan had received considerable royalties (which would exceed $2.8 million by 1974) from Sherwood and his wholly-owned corporation had successfully competed with Sherwood for several years (App. 270-271, 276, Tr. 1712, 1786).

The reference in appellants' brief to "threats of litigation against competitors" presumably refers to the single incident in which Sherwood's president, John Willman, called American Hospital Supply Corporation and complained that Sheridan was breaching the May, 1971 settlement agreement by selling "conductive line" tubing to the latter firm. The record pertaining to that single incident, set out in detail above (pp. 19-20, *supra*), hardly sustains the conclusion that either Brunswick or Sherwood was engaged in a program of "litigation and threats of litigation against competitors." The District Court gave the incident the full weight that it deserved when, in granting the motion for a directed verdict, he stated that "[a]t the most, I find in the evidence isolated incidents in which never could be

drawn, in my judgment, the conclusion that there was a deliberate attempt to monopolize. . . ." (App. 319, Tr. 2156).

Even if there were anything at all to the charges made in Part V of the appellants' brief, which there is not, Sheridan could have gotten to the jury only if he had offered evidence either (1) that Sherwood or Brunswick had acquired and intended to exercise the power to control price or exclude competition from a relevant market (*i.e.*, monopolization) or (2) that Sherwood or Brunswick specifically intended to obtain such power and embarked upon a course of conduct that created a dangerous probability of success (*i.e.*, attempted monopolization), *Kreager* v. *General Electric Co.*, *supra*, 497 F. 2d at 471. Sheridan offered no such evidence, so that the claims of bad faith conduct found in appellants' brief would not have gotten him to the jury on his Section 2 theory in any event.

The foregoing should be sufficient to dispose of this appeal. However, we now turn to other questions raised in appellants' brief, which we do not believe are necessary to the disposition of the appeal, but which we answer out of an abundance of caution.

III.

THE 1971 SETTLEMENT AGREEMENT DID NOT CONSTITUTE A MISUSE OF PLAINTIFFS' PATENT RIGHTS

Section 5(b) of the settlement agreement bars Sheridan and National Catheter from manufacturing or selling any product "similar to" the conductive tubing manufactured by Sherwood in 1969. Appellants argue that this provision only applies to products actually covered by Sheridan's patent issued in 1962, to which he had granted Brunswick an exclusive license. But if so construed the provision, which does not mention any patent, would have been entirely superfluous, prohibiting only conduct which would otherwise constitute an infringement of the patent or plaintiffs' exclusive license thereunder. Such infringement was also barred under Section 4, the immediately preceding section of the agreement. Thus, with respect to the conductive tubing

involved here, section 5(b) of the agreement was clearly intended to extend to some products not covered by the patent, but only to those "incorporating features or configuration of [a] . . . conductive line similar to the products manufactured by Sherwood as of February 1969." Section 5(b) did not apply to the number of other items Sheridan was then manufacturing and selling in competition with Sherwood.

Appellants contend, however, that if the agreement is so construed, it goes beyond the patent and, therefore, constitutes a patent misuse which violates the Sherman Act.

This argument disregards the inherent differences between the misuse of a patent on the one hand and the enforcement of a covenant not to compete on the other. A patent precludes anyone but the patentee from making or selling the patented device anywhere in the United States for the period prescribed by law. It thus gives the patentee a legal monopoly. To use a patent to extend this monopoly to unpatented products is unlawful. *International Salt Co.* v. *United States*, 332 U. S. 392 (1947).

A covenant not to compete by the seller of a business, by contrast, precludes competition by only one individual. When the sale of the business is combined with the employment of the seller by the new owner, a reasonable covenant not to compete will be upheld by the courts.[18] The public benefits to be derived from the enforcement of such covenants were recognized and described in then Circuit Judge Taft's classic opinion in *United States* v. *Addyston Pipe & Steel Co.*, 85 Fed. 271, 280 (6th Cir. 1898), *modified*, 175 U. S. 211 (1899):

> "After a time it became apparent to the people and the courts that it was in the interest of trade that certain covenants in restraint of trade should be enforced. It was of importance, as an incentive to industry and honest dealing

18. Whether the covenant in this case is reasonable is not before the Court at this time. As was shown above, the decision below was based upon Sheridan's inability to prove any "contract, combination or conspiracy" that restrained trade. The decision was not based upon a finding that the restraint was either reasonable or unreasonable.

in trade, that, after a man had built up a business with an extensive good will, he should be able to sell his business and good will to the best advantage, and *he could not do so unless he could bind himself by an enforceable contract not to engage in the same business in such a way as to prevent injury to that which he was about to sell.*" (Emphasis supplied.)[19]

The quotation from Judge Taft in the *Addyston Pipe* opinion is echoed by Lord MacMillan in *Vancouver Malt & Saki Brewing Co., Ltd.* v. *Vancouver Breweries, Ltd.* (1934) A. C. 181, 189 (P. C.) (B. C.), a case upon which appellants rely:

> "The law does not condemn every covenant which is in restraint of trade, for it recognizes that in certain cases it may be legitimate, and indeed beneficial, that a person should limit his future commercial activities, as, *for example, where he would be unable to obtain a good price on the sale of his business unless he came under an obligation not to compete with the purchaser. . . .*" (Emphasis supplied.)

A similar justification for covenants not to compete was more recently given by a respected commentator:

> "A transfer of good will cannot be effectively accomplished without an enforceable agreement by the transferor not to act so as unreasonably to diminish the value of that which he is selling." Blake, *Employee Agreements Not to Compete,* 73 Harv. L. Rev. 625, 646 (1960).

Such restrictions serve a public interest, and not merely the private interest protected by the covenant. A small businessman with ability or an invention would find it much more difficult to obtain substantial financial support and income from a larger enterprise if it knew that he could, after taking advantage of its

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19. See also *Day Companies, Inc.* v. *Patat,* 403 F. 2d 792, 796 (5th Cir. 1968), *cert. denied,* 393 U. S. 1117 (1969) (in order to enable [a seller] "to sell [something which he has obtained by skill] advantageously in the market, it is necessary that he should be able to preclude himself from entering into competition with the purchaser"); *Sound Ship Bldg. Corp.* v. *Bethlehem Steel Corp.,* 387 F. Supp. 252, 255 (D. N. J. 1975), *aff'd,* 533 F. 2d 96 (3d Cir. 1976); *Alders* v. *AFA Corp.,* 353 F. Supp. 654, 656 (S. D. Fla. 1973), *aff'd,* 490 F. 2d 990 (5th Cir. 1974).

resources, pull out at will and compete with it. If a purchaser of a company which was developing new products could not thus protect itself against competition by the owner of the company purchased, it would have little incentive to spend large sums both to compensate the seller and to create the facilities needed to manufacture the new products. Such discouragement of substantial investment in new products by those with sufficient capital would be harmful not merely to potential buyers and sellers, but to the public as well, which would be deprived of the benefit of earlier production and distribution of the new product on a large scale.

Brunswick's 1960 acquisition of Sheridan's enterprise illustrates the efficacy of a covenant not to compete. Brunswick constructed a "first-rate factory" across the road from Sheridan's barn which enabled Sheridan's products to be distributed on a broad scale (App. 51, Tr. 95). Within a few years, Sheridan's one-barn enterprise was converted into a business of substantial size from which he was deriving annual royalties of over $100,000, in addition to his salary and stock options. The royalties on the products produced under his patents had increased to $500,000 per year by 1975 (App. 270-271, Tr. 1712-1713).

Covenants not to compete customarily bar the seller-employee from competing with the purchaser, or from engaging in a broadly defined type of business.[20] "A typical restrictive covenant

20. Cases sustaining covenants against dealing in products "which compete" include *Eutectic Corp.* v. *Astralloy-Vulcan Corp.*, 510 F. 2d 1111, 1113 n. 1 (5th Cir. 1975) (covenant not to "render any services to any [competitor] dealing in materials, products or equipment . . . which compete with any materials, products or equipment which we . . . market . . ."); *Telecommunications, Engineering Sales & Service Co.* v. *Southern Telephone Supply Co.*, 518 F. 2d 392, 393 (6th Cir. 1975) (provision of technical assistance and equipment to independent telephone companies; covenant not to "sell or offer for sale competitive items of [employer] . . ."); *American Eutectic Welding Alloys Sales Co.* v. *Rodriguez*, 480 F. 2d 223 (1st Cir. 1973) (production and sale of welding and soldering alloys; covenant not to engage in any business dealing in "materials, products or

(Footnote continued on next page.)

prevent[s] the [franchisee], upon termination of the franchise agreement, from entering into *a similar* business, directly or indirectly, within a limited geographic area and time period." *Capital Temporaries, Inc.* v. *Olsten Corp.*, 506 F. 2d 658, 666 (2d Cir. 1974). (Emphasis supplied.) Other cases in this Court and elsewhere sustaining covenants like that here, which prohibits dealing in "similar" products, include *Syntex Laboratories, Inc.* v. *Norwich Pharmacal Co.*, 315 F. Supp. 45 (S. D. N. Y. 1970), *aff'd*, 437 F. 2d 566 (2d Cir. 1971) (covenant not to sell or manufacture *a product similar to* the one transferred); *In re Hale Desk Co.*, 97 F. 2d 372 (2d Cir. 1938) (covenant not to engage "in the desk business or in *any line of business similar to* that conducted by [purchaser-employer] . . ."); *Award Incentives, Inc.* v. *Van Rooyen*, 263 F. 2d 173, 174 (3d Cir. 1959) (covenant not to render "any services to any firm handling products or rendering services *similar to our products* . . .") (Emphasis supplied.)

Covenants not to compete serve to prevent competition by a seller or former employee where the restraint upon competition has in no way been legalized by the patent statute or any other statute. Yet they have been approved by the courts. The result should be no different when or because the agreement not to compete relates to an enterprise which has patents, at least when the covenant is not tied to the patents. Put another way, the

(Footnote continued from preceding page.)

equipment or a line of materials, products or equipment which compete with [those of the employer] . . . or engage in any *competing* business"); *Mixing Equipment Co.* v. *Philadelphia Gear, Inc.*, 436 F. 2d 1308, 1310 (3d Cir. 1971) (business of designing, manufacturing, and selling industrial mixing equipment; covenant not to engage in work "in any way connected with the development, manufacture or sale of any product which *competes* with any product of the [employer]."); *Wahlgren* v. *Bausch & Lomb Optical Co.*, 68 F. 2d 660, 662 n. 1 (7th Cir. 1934) (sale of optical equipment; covenant not to become engaged "in any . . . business *competing* with [employer] . . . or be interested in any . . . business engaged in the manufacture or sale of optical instruments or apparatus . . ."). (Emphasis supplied.)

covenant does not constitute the mis*use* of a patent when the covenant is not based upon the patent, and the patent has not been used to obtain the covenant. This was obviously true here, since the patent issued two years after the original (1960) covenant was agreed upon. The original covenant was based upon the purchase agreement and the employment relationship, and was designed, not to extend a patent, but to give the employer the benefits of what he had bought (App. 57, Tr. 125). The covenant in the May, 1971 settlement agreement was merely a modification of that original covenant.

The fact that a patent is obtained during the course of the employment, as was true of the 1962 conductive tubing patent here, does not change the nature of the pre-existing covenant not to compete, or mean that it becomes a patent misuse because it is not restricted to what is covered by a subsequent patent. The involvement of a patent will be fortuitous or irrelevant, as was the case here in 1960 before the 1962 conductive tubing patent issued. As Willman testified, it was Sheridan's know-how, not his patent rights, which were essential to success (App. 44-45, Tr. 79-80). In 1960 Sheridan had only a single patent on another kind of tubing as well as a few other patent applications on different kinds of tubing or catheters.

The entire concept of a covenant not to compete is that the employee or seller will not compete with the employer or buyer in the area in which they would be competitive. To narrow the covenant to the precise limits of a patent, which may not be nearly as broad as the competitive field which the purchase and employment agreements were designed to cover, would be to defeat the purpose of the covenant and of the legal theory upon which reasonable covenants are upheld.

In the cases relied on by appellants in Part I of their brief, the restrictions on competition were contained in patent licenses, and were not primarily ancillary to the sale of a business and an employment agreement.

Appellants cite cases in which a patent licensing contract itself prohibited the licensee from selling products in competi-

tion with or similar to the patented product. *McCullough* v. *Kammerer Corp.*, 166 F. 2d 759 (9th Cir.), *cert. denied,* 335 U. S. 813 (1948); *Krampe* v. *Ideal Industries, Inc.*, 347 F. Supp. 1384 (N. D. Ill. 1972). This, of course, would be a bare attempt to extend the effect of a patent monopoly. The cases did not involve a restraint ancillary to the purchase of a business accompanied by an agreement to employ the prior owner. Similarly, in *Agrashell, Inc.* v. *Hammons Products Co.*, 479 F. 2d 269 (8th Cir.), *cert. denied,* 414 U. S. 1022 (1973), the agreement in question bound the buyer to handle only the patented product for three years after the expiration of the patent; again, there was nothing making the covenant ancillary to a purchase or employment agreement.

In *Compton* v. *Metal Products, Inc.*, 453 F. 2d 38 (4th Cir. 1971), *cert. denied,* 406 U. S. 968 (1972), the patent licensee agreed in the license agreement not to manufacture or sell any equipment "of the type licensed." After concluding that this went beyond the protection of the patent law and would violate the Sherman Act, the court dealt with the finding below that this was a covenant not to compete as part of "the sale of a going business." The court rejected

> "this view of the agreement, especially since the parties themselves apparently viewed it *as a license, not as a contract for the sale of a business. . . .*" Id. at 45. (Emphasis supplied.)

Here there can be no doubt that the covenant was ancillary to the purchase and employment agreements, Although there was a contemporary patent license, it did not extend to the product here involved, which was covered by a patent application filed and granted thereafter and assigned to Brunswick in a subsequent license after Sheridan had become a Brunswick employee.

The *Compton* opinion then proceeded to assume that the contract was to be judged as a covenant not to compete ancillary to the sale of a business. It concluded that:

> "[T]he total withdrawal of Compton from the *mining machine manufacturing business,* or even from the *auger manufacturing business,* everywhere in the world for a

period of 20 years unreasonably lessens the competition which the public has a right to expect, and constitutes misuse of the patents." *Id.* (Emphasis supplied.)

Here, on the other hand, the restriction, as narrowed by the 1971 settlement agreement, applied only to a few specifically defined products, not an entire line of business, for a period of five years. The five-year restriction in the 1971 agreement was a reduction of the period covered by the 1960 covenant, not an extension of it. Appellants do not assert that five years is an unduly long period; indeed, it is quite common and has frequently been upheld.[21] Sheridan was willing to accept a five-year restriction not only in the 1971 agreement with appellees but again in 1974 when National Catheter Corporation was sold to the Mallinckrodt Corporation (App. 275, Tr. 1756-1757).

Appellants also do not contend that the covenant is too broad because it lacks a territorial limitation. Appellants' brief (Part V) admits that the tubing is marketed "on a national basis," and there is no evidence that the parties understood the covenant to operate more broadly or that appellees have sought to enforce it or claim damages for conduct outside the United States. Many cases have held that the proper scope of a restriction is the area in which the party to be protected markets the product in question, even if that area be nationwide or even worldwide.[22]

21. *In re Hale Desk Co.*, 97 F. 2d 372 (2d Cir. 1938) (5 years); *Nat'l Homes Corp.* v. *Lester Industries, Inc.*, 404 F. 2d 225 (4th Cir. 1968) (10 years); *Day Companies, Inc.* v. *Patat*, 403 F. 2d 792 (5th Cir. 1968), *cert. denied*, 393 U. S. 1117 (1969) (5 years); *Wahlgren* v. *Bausch & Lomb Optical Co.*, 68 F. 2d 660, 662 (7th Cir. 1934) (5 years); Annot., 45 A. L. R. 2d 77 (1956); Annot., 41 A. L. R. 2d 15 (1955).

22. *DeLong Corp.* v. *Lucas*, 176 F. Supp. 104, 121-22 (S. D. N. Y. 1958), *aff'd*, 278 F. 2d 804 (2d Cir. 1960), *cert. denied*, 364 U. S. 833 (1960) (the world); *Alders* v. *AFA Corp.*, 353 F. Supp. 654, 658 (S. D. Fla. 1973), *aff'd*, 490 F. 2d 990 (5th Cir. 1974) (United States and Canada); *Mixing Equip. Co.* v. *Philadelphia Gear, Inc.*, 436 F. 2d 1308, 1314 (3d Cir. 1971) (no geographical limitation); *Day Companies, Inc.* v. *Patat*, 403 F. 2d 792, 794 (5th Cir. 1968), *cert. denied*, 393 U. S. 1117 (1969) (the territory covered by the transferred

(Footnote continued on next page.)

IV.

THE DOCTRINE OF ANCILLARY RESTRAINTS SUPPORTS THE COVENANTS AT ISSUE HERE

Parts II, III, and IV of the appellants' brief are devoted to a discussion of why the doctrine of ancillary restraints is not applicable to the instant case. In one respect, this statement is correct, because the District Court did not rely upon that doctrine in taking the case away from the jury. As we have shown, the decision below was based upon Sheridan's inability to prove either a "contract, combination or conspiracy" that restrained trade or a claim of monopolization or attempted monopolization—not upon a finding that the doctrine of ancillary restraints applies. Nevertheless, we do not wish appellants' treatment of the subject to go unanswered.

A. The 1971 Settlement Must Be Viewed in Light of the 1960 Agreement

In part II of their brief, appellants treat the 1971 settlement agreement as if it were a naked agreement between competitors to discontinue competition in similar products. Our position is that the settlement is not to be viewed merely in the abstract or *in vacuo,* but in the context of the dispute it was designed to resolve. We have not made the contention that the mere fact that a restriction on competition is incorporated into a settlement makes it lawful "without an ancillary restraints analysis." (Appellants' Br. Part III-C). The point here is that the 1971 agreement was a settlement of an ancillary restraints dispute. Accordingly, it should be upheld if it is an appropriate dispo-

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business); *Continental Group, Inc.* v. *Kinsley,* 422 F. Supp. 838, 841 (D. Conn. 1976) (U. S., Canada, Western Europe, and Japan); *Trans-American Collections, Inc.* v. *Continental Account Servicing House, Inc.,* 342 F. Supp. 1303, 1305 (D. Utah 1972) (U. S.); *Burton, Parsons & Co.* v. *Parsons,* 146 F. Supp. 114, 116 (D. D. C. 1956) (the world); Annot., 46 A. L. R. 2d 119, §§ 174, 192, 194 (1956); Annot., 43 A. L. R. 2d 94, §§ 109, 125, 147 (1955).

sition of the controversy caused by the 1960 purchase and employment agreements and the covenant contained therein.

The courts have often said that disposition of litigation by agreement of the parties is "a course long favored by the law." *Weight Watchers of Philadelphia, Inc.* v. *Weight Watchers International, Inc.*, 455 F. 2d 770, 773 (2d Cir. 1972); *Williams* v. *First National Bank*, 216 U. S. 582, 595 (1910). "It hardly seems necessary to point out that there is an overriding public interest in settling and quieting litigation." *Van Bronkhorst* v. *Safeco Corp.*, 529 F. 2d 943, 950 (9th Cir. 1976). This policy includes the settlement of antitrust claims. *S. E. Rondon Co.* v. *Atlantic Richfield Co.*, 288 F. Supp. 879 (C. D. Cal. 1968); *Richard's Lumber & Supply Co.* v. *United States Gypsum Co.*, 545 F. 2d 18, 20 (7th Cir. 1976), *cert. denied*, 97 S. Ct. 1326 (1977); *Three Rivers Motor Co.* v. *Ford Motor Co.*, 522 F. 2d 885 (3d Cir. 1975).

As this Court knows, the magnitude of the case load now confronting the Federal Courts makes it all the more desirable that settlements be encouraged. Thus, the courts should be reluctant to reopen a settled controversy. "A party by settlement may surrender rights that the law would have sustained, but that is no reason for disregarding the settlement." *A. D. Juilliard & Co.* v. *Johnson*, 259 F. 2d 837, 843 (2d Cir. 1958); *Hennessy* v. *Bacon*, 137 U. S. 78, 85 (1890).

In the context of this case that means that disputes as to whether the 1960 covenant was or was not reasonable, or as to whether Sheridan quit Brunswick of his own accord or was pushed, are not now to be judicially redetermined. It does not, however, bar determining the validity of the 1971 settlement as a lawful disposition of the 1960 controversy.

The decision of the Seventh Circuit (per Stevens, J.) in *Business Forms Finishing Service, Inc.* v. *Carson*, 452 F. 2d 70 (7th Cir. 1971), is entirely consistent with and indeed supports this analysis. The case was concerned with a consent order in a patent infringement suit in which the defendant "agreed to recognize the validity of plaintiff's patent" *Id.* at 73. The Court held that Supreme Court decisions rendered the "agreement

to accept the validity of plaintiff's patent . . . unenforceable." *Id.* at 75. *Lear, Inc.* v. *Adkins,* 395 U. S. 653 (1969); *Blonder-Tongue* v. *University of Illinois Foundation,* 402 U. S. 313 (1971). The opinion referred to covenants not to compete as analogous, but recognized that "if limited and ancillary to a valid business purpose" they may be lawful, and then commented that the "desirability of settling a lawsuit would not *in itself* establish sufficient justification for such an agreement." 452 F. 2d at 73-74. (Emphasis supplied.) The desirability of settling a lawsuit arising out of a covenant not to compete should, however, validate a settlement agreement which furnishes an appropriate resolution of the original controversy.

Appellants also assert that the time span between 1960 and 1971 in itself precludes treatment of the 1971 agreement in relation to its 1960 predecessor. But the 1960 agreement clearly was in effect in October 1967 when Sheridan decided to terminate his connection with Brunswick. Brunswick promptly brought suit in 1968, and the litigation was pressed until the eve of trial in 1971 when the settlement was entered into. There is no reason why, under these circumstances, the passage of time should have the effect of forfeiting Brunswick's rights.

Finally, appellants assert that neither Sherwood nor National Catheter, both of whom were parties to the 1971 agreement, had anything to do with the 1960 transactions, as, of course, they could not, for they were not in existence at that time. But the fact that Brunswick in 1967 established Sherwood as its medical supply subsidiary and that Sheridan established National Catheter, of which he was the founder and principal shareholder, does not mean that the 1960 agreements would not apply to these corporations, or that they were not proper parties to a suit based upon those agreements or to its settlement. A person subject to restrictions under a contract cannot evade them by creating a controlled corporation to do what he has agreed not to do. The 1960 covenants thus could not be evaded by either party by the creation of subsidiaries or controlled

corporations. *New Colonial Ice Co.* v. *Helvering*, 292 U. S. 435, 442 (1934); *Bangor Punta Operations, Inc.* v. *Bangor & Aroostook R. R.*, 417 U. S. 703, 713 (1974); H. Ballantine, Ballantine on Corporations 304 (1946).[23] Cases involving covenants not to compete include *Universal Electric Corp.* v. *Golden Shield Corp.*, 316 F. 2d 568 (1st Cir. 1963); *Structural Dynamics Research Corp.* v. *Engineering Mechanics Research Corp.*, 401 F. Supp. 1102, 1118 (E. D. Mich. 1975).

Furthermore, it was entirely appropriate for Brunswick to join Sherwood, which had taken over its medical supply activities, as a plaintiff, and to join National Catheter, the company through which Sheridan was, in Brunswick's view, violating the 1960 covenant, as a defendant in its suit to enforce that covenant.

B. There Is No Evidence That Brunswick's Dominant Purpose Was to Eliminate Competition

Appellants argue that the doctrine of ancillary restraints has no applicability here. They assert, in the first place (Br. Part II-A), that the doctrine is inapplicable because the dominant purpose of Brunswick (or Brunswick and Sherwood) was to eliminate competition. This is an example of appellants' failure to recognize that the 1971 settlement agreement must be read in the context of the dispute which it was designed to settle. Clearly, in 1960, when Brunswick agreed to purchase a small enterprise, with which it did not compete, so that it could develop and distribute on a much larger scale the products which Sheridan was then producing, and others which he might develop and invent, the dominant purpose and effect was not to eliminate competition but to create it. And this is so even though the purpose and effect would be to develop new products which might be patented and thus subject to commercial manufacture

23. See also *Doyn Aircraft, Inc.* v. *Wylie*, 443 F. 2d 579, 584 (10th Cir. 1971); *Allied Chemical Corp* v. *Randall*, 321 F. 2d 320, 323 (7th Cir. 1963); *Francis O. Day Co.* v. *Shapiro*, 267 F. 2d 669, 673 (D. C. Cir. 1959).

and distribution by no one else. If such a purpose were regarded as anti-competitive, every effort to develop new and useful products might be suspect under the antitrust laws.[24]

Obviously, in 1960 when the conductive tubing here involved had not even reached the point of a patent application, appellees' purpose with respect to it could not have been said to be improperly anti-competitive.

Appellants place a great deal of emphasis on the fact that, at the time of the settlement agreement, 3½ years after Sheridan had left Brunswick, he no longer possessed Brunswick's confidential trade secrets or technical know-how. They also argue (Br. Part III-B) that the 1960 employment agreement was invalid because its purpose was not to protect Brunswick's trade secrets, know-how and customers lists, since the flow of information was from Sheridan to Brunswick, not the reverse. But this argument ignores the fact that the covenant was ancillary, not only to an employment agreement, but to the sale of a business as well. Under these circumstances, Sheridan's secrets and know-how became Brunswick's, and Brunswick could reasonably bar Sheridan from using that information in competition with it for a reasonable period of time.

The 1960 Employment Agreement (App. 372, Pls. Ex. 5) required Sheridan to promptly disclose all inventions and assist Brunswick in prosecuting patent applications (¶ 5), and prohibited him from disclosing to others "any technical know-how, data, or other information, relating to inventions, improvements, secret processes and formulas . . . or any confidential information" acquired in the course of his employment (¶ 6).

Sheridan was recognized as a leading innovator in his field, and research and development of new products was his principal

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24. Appellants' efforts to demonstrate anti-competitive behavior by Sherwood include a quotation from an exhibit (App. 579, Def. Ex. BT) which the District Court ruled to be inadmissible (See Br. note 15). Of course, appellants have no right to rely upon a document that was excluded from evidence, and as a result the quotation from Exhibit BT should be disregarded.

activity during his employment at Brunswick; thus, he obviously was privy to the trade secrets and other confidential information referred to in the 1960 Agreement. Brunswick was entitled to the fruits of research conducted by Sheridan for which it paid and supplied facilities. The 1971 Settlement Agreement (App 387, Pls. Ex. 9) protected Brunswick by reaffirming Sheridan's obligation not to disclose trade secrets acquired by him "during his employment by or his confidential relationship to Brunswick" (¶ 16).

The facts in the instant case are strikingly similar to those in *Koehler* v. *Cummings,* 380 F. Supp. 1294, 1299 (M. D. Tenn. 1971, as amended 1974), where a covenant not to compete was upheld:

> ". . . The major asset of [the acquired company], all parties agree, was the man Jamul and his ideas. This essentially constituted the basis for investment by all parties."
>
> "The danger to the employer . . . has already been seen. [The employer] had one valuable asset, the ideas of the [employee]. About $30,000 was allegedly invested . . . to develop these ideas. . . . Since these men were certainly not inexperienced in business ventures, it can only be concluded that . . . these ideas were believed to have great potential. The key to this potential was [the employee]." *Id.* at 1306.
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> * * * * *
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> ". . . The threatened danger to the employer . . . lay in experiencing competition from its own former idea man, against which the covenant protected it." *Id.* at 1307.
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> * * * * *
>
> ". . . Where a covenant not to compete was entered into by an idea man, the principal asset of a corporation in a highly technical and specialized field, it seems inescapable that, in an effort to protect the investments by the corporation and by the plaintiff Koehler, the covenant was not unreasonable, though broad in its territorial limitation." *Id.* at 1309.

In any event, the controversy as to whether the 1960 covenant was lawful was disposed of, without judicial resolution, in the

1971 settlement. The fact that Sheridan had terminated his employment in 1967 did not mean that it was inappropriate or unlawful to settle the controversy, which arose because of his violation of the 1960 covenant, by a specific narrower restriction which extended for five years after the date of the settlement instead of five years after the termination of the period in which Brunswick might employ him under the 1960 employment agreement.

Appellants' attempt to analogize this case to the well-known antitrust cases of *United States* v. *American Tobacco Co.*, 221 U. S. 106 (1911), and *Schine Chain Theatres* v. *United States*, 334 U. S. 110 (1948), is indeed far-fetched. In both of those cases there was a mass of evidence that trade was restrained or monopolized pursuant to plan. Covenants not to compete or settlement agreements were condemned "as part of an unlawful scheme" of broad magnitude, and were not "isolatedly viewed," *American Tobacco, supra*, 221 U. S. at 183, quoted in Part II-A of appellants' brief. The passage from *Schine* quoted on the same page recognizes that agreements not to compete have at times been "used as a weapon in restraint of trade or in an effort to monopolize," and that

> ". . . . against the background of Schine's other monopolistic practices, it seems to us that the District Court might infer that the requisite purpose was present and that these agreements were additional weapons in Schine's arsenal of power. . . ." 334 U. S. at 119.

But the Court also noted that

> "If we had here only agreements not to compete, the inferences drawn by the District Court might not be warranted." *Id.*

All we have here is a covenant not to compete, greatly narrowed by a settlement of the original controversy. This is a far cry from the industry-wide conspiracies in many of the cases appellants cite.

Appellants also emphasize the decisions of the District Court granting a preliminary injunction in *Lektro-Vend Corp.* v.

Vendo Co., 403 F. Supp. 527 (N. D. Ill. 1975), *aff'd*, 545 F. 2d 1050, 1052, 1059 (7th Cir. 1976), *rev'd on other grounds*, 97 S. Ct. 2881, 53 L. Ed. 2d 1009 (1977), and of the Privy Council in *Vancouver Malt & Saki Brewing Co. Ltd.* v. *Vancouver Breweries, Ltd.* (1934), A. C. 181 (P. C.) (B. C.). Both of these cases, however, found that the principal object of the contracts in issue was to eliminate competition, not the purchase or employment agreements to which the restrictive covenant was supposed to be ancillary. In *Lektro-Vend* the District Court gave special weight to the fact that: "Since Mr. Stoner apparently was never called upon to perform significant services for Vendo the covenant amounted to a naked agreement not to compete, solely anticompetitive in purpose and effect." 403 F. Supp. at 533.

In *Vancouver*, although the contract recited that the purchase was of the vendor's goodwill from his liquor license as it related to beer, the court found that in fact there was no purchase at all; the purchasing company, which brewed beer, paid the seller, which brewed sake but not beer, to agree not to brew beer. "Nothing has been sold." There was merely "a bare covenant not to compete" such as the English courts have never upheld. (1934) A. C. at 190.

Here, on the other hand, there can be no doubt that the purchase of Sheridan's business and his employment by Brunswick were the principal objects of the 1960 agreements. Brunswick took over and greatly expanded the business, and Sheridan was a valuable employee for seven years, until he quit.

C. There Is No Evidence That Brunswick Possessed Monopoly Power in a Relevant Market

Appellants also assert that appellees' possession of monopoly power precludes reliance upon the ancillary restraints doctrine. As was pointed out in our discussion of appellants' argument based on Section 2 of the Sherman Act (Point II, *supra*), the difficulty with this argument is that there is no evidence that

Brunswick possessed monopoly power either in 1960 or 1971. The mere possession of 100% of the market in the context of development of a new product without the power to control prices or exclude competition is not sufficient to establish such power—and that is all the appellants can rely on, since they introduced no evidence showing price or market control. *Cf. United States* v. *Grinnell,* 384 U. S. 563, 571 (1966); *International Railways* v. *United Brands Co.,* 532 F. 2d 231, 239 (2d Cir.), *cert. denied,* 97 S. Ct. 101 (1975).[25]

D. There Is No Evidence That Enforcement of the Covenant Would Have Harmed the Public

Appellants also argue that the ancillary restraints doctrine is inapplicable because the alleged superiority of their product means that the public would be harmed if they were barred from producing and selling it. As would be expected, their witness testified that their product was superior. He was able to make the Sherwood tubing leak at the joint by pinching off one end, immersing the tubing in Kool-Aid, and blowing air in the other end (App. 182-183, Tr. 1084-1085). The same witness admitted on cross-examination that this would be an "idiotic thing" to do in an operating room (App. 191, Tr. 1130). The same witness was able to cause a "spark gap" in the Sherwood tubing at the joint by connecting a 50,000 volt generator (Pls. Ex. 61 for id.) to the conductive portion of the tubing (App. 172-175, Tr. 1074-1077), though admitting on cross-examination that anyone who brought such a device into the operating room should be "thrown in jail" (App. 187-190, Tr. 1101-

25. *Bascom Launder Corp.* v. *Telecoin Corp.,* 204 F. 2d 331, 335 (2d Cir.), *cert. denied,* 345 U. S. 994 (1953), cited by appellants (Br. Part II-B), did not involve a covenant not to compete ancillary to agreements to purchase or employ, but the different problem of when an exclusive distributorship becomes unlawful. Such an exclusive arrangement has the effect of precluding competition generally and not merely that of a single individual who, in connection with the sale of his business, has agreed not to compete with the buyer for a limited time.

1104). The witness was unable to compare the 50,000 volts generated by this device to the minute voltages generated by the manual handling of suction tubing in the operating room (App. 191, Tr. 1109).

Sheridan also claims, completely without supporting testimony or exhibits, that Sherwood's tubing is implicated in a "microshock" hazard having to do with cardiac arrest. If there were anything to this very serious charge one certainly would have expected evidence to support it.

It is therefore obvious that Sheridan's assertion that the Sherwood tubing leaks in use, presents serious dangers that inflammable gases might still explode, or that the tubing might cause cardiac arrest are pure speculation; there is no evidence in the record that Sherwood's tubing ever presented any danger in normal use in the operating room.

But in any event, for the reasons referred to above (*supra*, pp. 31-33), the fact that a restrictive covenant might for a period preclude the sale of even a superior product (which Sheridan's was not shown to be) by the covenantor does not mean that the covenant becomes void. The public interest must be looked at more broadly. In the long run, the public benefits from the development of new devices and products on a large scale by those with resources to do so. In many situations, such as the case at bar, the development of a new and better device would have been retarded or discouraged if the inventor had been unable to join with a larger organization with ample resources and capital. And such an organization would be much less likely to be interested if the inventor could, as appellants insist, take leave of the purchasing enterprise and immediately set up a competing business.

Appellants also urge that Brunswick is preventing not only Sheridan from exercising his skill in competition with it but also Isaac Jackson, the inventor of the conductive tubing produced by Sheridan's company, National Catheter. Sheridan's covenant

with Brunswick (either in 1960 or 1971) did not preclude Jackson from marketing his slightly different form of "conductive line" tubing. If Jackson had assigned, licensed or sold his tubing to anyone but Sheridan or Sheridan's company, the restrictive covenant with Brunswick would have been totally inapplicable. It was not the covenant with Brunswick which required the employees of Sheridan or National Catheter to turn their inventions over to him or his company, but the arrangement which they made among themselves.[26]

26. Of course, Sheridan or his company could not have evaded the covenant by themselves arranging for an employee, for their benefit, to engage in the conduct prohibited by the restrictive covenant, which applies to anything that they do "directly or indirectly." See p. 40, *supra*. It may be noted that the record here indicates that Sheridan arranged for the patenting of Jackson's device by the attorney who had previously represented Sheridan, and who testified that he knew Sheridan but not Jackson (App. 157-158, Tr. 1016-1017).

CONCLUSION

In directing a verdict in favor of Sherwood and Brunswick, and speaking of the evidence presented at trial, Judge Foley said that there "never could be drawn, in my judgment, the conclusion that there was a deliberate attempt to monopolize, or to unreasonably restrain trade" (App. 319, Tr. 2156). The discussion above, particularly that contained in Points I and II, shows that the record fully supports the conclusion of the trial court. For that reason, the order directing a verdict in favor of Sherwood and Brunswick as to Count I of Defendants' Amended Counterclaim should be affirmed.

Appellants having abandoned their appeal with respect to Counts III and IV of the Amended Counterclaim, the directed verdict should be affirmed as to those counts as well.

Respectfully submitted,

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CERTIFICATE OF SERVICE

I hereby certify that two copies of the foregoing Brief for Appellees were mailed, first class postage prepaid, this 31st day of October 1977 to John P. Arness, Esquire, Hogan & Hartson, 815 Connecticut Avenue, Washington, D. C., 20006, counsel for appellants.

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